

DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS: 06-0508
Indiana Sales and Use Tax
For the Tax Periods 2003, 2004

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ISSUES

I. Processing Exemption – Sales/Use Tax.

Authority: IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-2.5-5-1 et seq.; IC § 6-2.5-5-3(b); *Indianapolis Fruit Co. v. Department of State Revenue*, 691 N.E.2d 1379 (Ind. Tax Ct. 1998); 45 IAC 2.2-5-8.

Taxpayer maintains that particular items of kitchen equipment – prep tables, work tables, and equipment stands – qualify for the processing exemption.

II. Refrigeration Equipment – Sales/Use Tax.

Authority: 45 IAC 2.2-5-8; *Indianapolis Fruit Co. v. Department of State Revenue*, 691 N.E.2d 1379 (Ind. Tax Ct. 1998); Sales Tax Information Bulletin 55 (May 31, 1989).

Taxpayer asserts that it uses certain items of its restaurant kitchen equipment – prep tables, work tables, and equipment stands – to support production or “work-in-process” equipment, which entitles taxpayer to the exemption. Taxpayer also asserts that it uses its freezer/cooler units to temporarily store work-in-process materials, and thus entitles taxpayer to the exemption.

STATEMENT OF FACTS

Taxpayer is a horse racing operation consisting of both live and simulcast wagering. In addition to its onsite horse racing track and facility, taxpayer also operates two satellite-wagering facilities. Each of taxpayer's three facilities includes a restaurant.

Over the course of an audit covering tax years 2003 and 2004, the Department reviewed taxpayer's records regarding construction of, and acquisition of capital equipment for, the three restaurants.

The review of taxpayer's transactions resulted in proposed additional assessments of Indiana sales and use tax. Taxpayer originally protested those additional assessments by filing refund claims. After the Department rejected taxpayer's refund claims, taxpayer filed a protest against

the proposed assessments. While taxpayer's assertions addressed multiple equipment purchases, the Department limited the scope of any hearing regarding taxpayer's assertions to the items referenced herein; the Department gave no indication that the auditor's conclusions with respect to excluded items were erroneous or that those conclusions would be revisited. An administrative hearing was held, in which taxpayer again protested the sales and use tax assessments on both the items referenced herein and the additional items excluded from the scope of the hearing.

I. Processing Exemption – Sales/Use Tax.

DISCUSSION

Indiana imposes a sales tax on retail transactions. IC § 6-2.5-2-1. The state also imposes a complementary use tax on tangible personal property that is stored, used, or consumed within the state. IC § 6-2.5-3-2. For both of these taxes, certain exemptions are available. IC § 6-2.5-5-1 et seq. Taxpayer invokes the equipment exemption found at IC § 6-2.5-5-3(b), which reads as follows:

Transactions involving manufacturing machinery, tools, and equipment are exempt from the state gross retail tax if the person acquiring that property acquires it for direct use in the direct production, manufacture, fabrication, assembly, extraction, processing, refining, or finishing of other tangible personal property.

Taxpayer maintains that its prep tables, work tables, and equipment stands are entitled to this exemption because the prep and work tables are used by Taxpayer's restaurant kitchen personnel to support the preparation of various food items; and the equipment stands are used to support various pieces of production equipment, including mixers, slicers, and food processors. In support of that assertion, Taxpayer cites to 45 IAC 2.2-5-8 (c)(2)(E), which provides that equipment that "constitute[s] essential and integral parts of the integrated production process" are exempt from state gross retail tax.

"Without production there can be no exemption." *Indianapolis Fruit Co. v. Department of State Revenue*, 691 N.E.2d 1379, 1384 (Ind. Tax Ct. 1998). The processes examined in *Indianapolis Fruit* included operations in a 'garden cut' facility where employees cleaned, cut, and packaged fruits and vegetables for resale by restaurants and grocery stores. Indianapolis Fruit required its employees in that facility to wear protective clothing "to ensure that its facility meets or exceeds applicable state and federal standards concerning contamination of food for human consumption." *Id.* Taxpayer's operations include processes similar to those documented in *Indianapolis Fruit*. Shortly after the hearing, per the Department's request, taxpayer provided photographs showing prep tables, work tables, and equipment stands in its restaurant kitchen areas. Taxpayer uses its prep tables and work tables to cut and prepare various raw food products and materials; to mix food products in preparation for cooking and meal service; and for temporary storage of food items off of the kitchen floor. One of the examples given in 45 IAC 2.2-5-8 (c)(2)(E) describes a "work bench used in conjunction with a work station or which supports production machinery within the production process."

As in *Indianapolis Fruit*, the work tables and prep tables are integral in ensuring that kitchen employees prepare meals—the taxpayer’s restaurant’s production process--that presumably meet applicable state and federal standards concerning preparation of meals for human consumption. This same analysis also applies to taxpayer’s equipment stands, which enable the taxpayer’s kitchen employees to use various machines necessary for meal preparation.

Accordingly, to the extent that taxpayer’s prep tables, work tables, and equipment stands are employed *within* the production process occurring in its restaurant kitchen facilities, the prep tables, work tables, and equipment stands are entitled to exempt treatment.

FINDING

As to taxpayer’s work tables, prep tables, and equipment stands, taxpayer’s protest is sustained.

II. Refrigeration Equipment – Sales/Use Tax.

DISCUSSION

Taxpayer’s restaurant kitchen facilities include walk-in cooler/freezer units. These units house both a cooler element and a freezer element. Taxpayer asserts that it uses the cooler element (or section) exclusively to temporarily store work-in-process. Taxpayer includes the shelving as part of the cooler section for its tax-exempt claim, asserting that the shelving is used to support the work-in-process that is temporarily stored in the cooler section. Taxpayer maintains that the cooler section and shelving used to temporarily store work-in-process is essential and integral to an integrated process and, therefore, is exempt under 45 IAC 2.2-5-8(e)(1). The regulation, in relevant part, states that “[t]angible personal property used in or for the purpose of storing work-in-process or semi-finished goods is not subject to tax if the work-in-process or semi-finished goods are ultimately completely produced for resale and in fact resold.” 45 IAC 2.2-5-8(e)(1)

The Indiana Department of Revenue Sales Tax Information Bulletin #55 (May 31, 1989) is instructive:

Restaurant food heating or cooling is taxable unless it is used in the actual production and creation of food. Utilities used for warming tables and refrigeration areas are taxable unless the food is undergoing a change due to this process. **Refrigeration for storage is a taxable use** of the utilities. . . . Utilities serving a refrigerator . . . used to keep the products or the raw materials in the same condition are taxable. **[Emphasis added]**

In contrast to taxpayer’s photographs displaying work tables, prep tables, and equipment stands as an integral part of the production of meals, taxpayer’s photos of the door of one of the cooler/freezer units and (presumably) the contents stored within one of the cooler/freezer units does little to contradict the auditor’s finding. The audit report was based on the auditor’s personal observation of how the taxpayer used its coolers and freezers. The auditor observed that the taxpayer used the coolers and freezers to store food, not to produce or create food. Taxpayer has failed to establish that the taxpayer uses its cooler/freezer units to store work in process.

In the absence of a finding that the taxpayer is producing or processing tangible personal property, there can be no “work-in-progress” and the related equipment will not qualify for the exemption. *Indianapolis Fruit*, 691 N.E.2d at 1384.

FINDING

Taxpayer’s protest is respectfully denied.

LM/WL/DK – July 23, 2007